IN THE SUPREME COURT OF PENNSYLVANIA
MIDDLE DISTRICT

No. 47 MAP 2018

COMMONWEALTH OF PENNSYLVANIA,

Appellee,

v.

JOSEPH PETRICK,

Appellant.

BRIEF OF AMICUS CURIAE THE NATIONAL CONSUMER BANKRUPTCY RIGHTS CENTER, THE AMERICAN CIVIL LIBERTIES UNION OF PENNSYLVANIA, INC., PENNSYLVANIA LEGAL AID NETWORK, INC., COMMUNITY LEGAL SERVICES, INC., NEIGHBORHOOD LEGAL SERVICES ASSOCIATION, THE COMMUNITY JUSTICE PROJECT AND THE NATIONAL CONSUMER LAW CENTER IN SUPPORT OF PETITIONER

Appeal from Order of the Superior Court at No. 619 MDA 2017, dated February 20, 2018, Affirming the Judgment of Sentence of the Court of Common Pleas of Lackawanna County dated March 8, 2017.

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Amici curiae are nonprofit organizations that represent and promote the rights of low-income consumers in cases involving debt collection and other consumer matters. *Amici* have a special interest in, and substantial expertise regarding, debt collection litigation and low-income consumers in Pennsylvania.

The National Consumer Bankruptcy Rights Center ("NCBRC") is a nonprofit organization dedicated to preserving the bankruptcy rights of consumer debtors and protecting the bankruptcy system's integrity. The federal Bankruptcy Code grants financially distressed debtors' rights critical to the bankruptcy system's operation. Yet consumer debtors with limited financial resources are often ill-equipped to protect their rights within that system, particularly in the appellate process. NCBRC files amicus curiae briefs in systemically-important cases to ensure that courts have a full understanding of the applicable bankruptcy law, the case, and its implications for consumer debtors.

The American Civil Liberties Union ("ACLU") is a nationwide, nonprofit, nonpartisan organization of over 1.75 million members. Since its founding in 1920, the ACLU has been dedicated to preserving and defending the principles of individual liberty and equality embodied in the United States Constitution and civil rights laws. The American Civil Liberties Union of Pennsylvania, Inc. is one of the organization's state affiliates, with over 30,000 members throughout Pennsylvania.

The ACLU of Pennsylvania has particular expertise regarding the assessment and collection of fines, costs, and restitution in criminal cases throughout the state. Just this year, the Superior Court issued published opinions in three appeals brought by the ACLU of Pennsylvania, invalidating trial court practices that led to the unlawful incarceration of dozens of defendants each month solely for failure to pay court debt. *See Commonwealth v. Mauk*, 185 A.3d 406, (Pa. Super. Ct. 2018), *Commonwealth v. Diaz*, 191 A.3d 850 (Pa. Super. Ct. 2018), and *Commonwealth v. Smetana*, 191 A.3d 867 (Pa. Super. Ct. 2018).

The Pennsylvania Legal Aid Network, Inc. ("PLAN"), Community Legal Services, Inc. ("CLS"), Neighborhood Legal Services Association ("NLSA"), and the Community Justice Project ("CJP") provide free civil legal representation, advice, and education to low-income individuals and families throughout Pennsylvania. CLS, NLSA, and CJP provide direct services to hundreds of low-income debtors every year seeking to file bankruptcy cases to get a fresh start and rebuild their lives after serious financial set-backs. PLAN is the state's coordinated system of civil legal aid and provides funding to legal aid providers statewide, coordinates trainings for public interest lawyers, and leadership for legal aid providers. Together, these legal aid *amici* are interested in this case because of the significant impact it could have for the low-income consumers they represent.

The National Consumer Law Center is a public interest, nonprofit legal organization incorporated in 1971. It is a national research and advocacy organization focusing specifically on the legal needs of low income, financially distressed and elderly consumers. NCLC draws on over forty years of expertise to provide information, legal research, and policy analysis to Congress, state legislatures, administrative agencies, and courts.

INTRODUCTION

The resolution of this matter requires the navigation of two important but competing legal principles. On the one hand, a discharge in bankruptcy does not operate to discharge a previously ordered criminal restitution obligation imposed for rehabilitative purposes. *See Kelly v. Robinson*, 479 U.S. 36 (1986). On the other hand, a State's police and regulatory power may not be used as a means for private entities to collect debts that have been discharged in bankruptcy. *See Perez v. Campbell*, 402 U.S. 637 (1972) (state statute impermissibly conditioned drivers' license on the satisfaction of a discharged tort obligation owed to private individuals). Congress balanced these competing principles when it enacted section 523(a)(7) of the federal Bankruptcy Code ("Bankruptcy Code" or "Code"), which provides that a debt is nondischargeable to the extent it is "for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss." 11 U.S.C. § 523(a)(7). As section 523 illustrates, a fine payable to *and* for the benefit of a State (*e.g.*, to serve a rehabilitative purpose of the State) is nondischargeable, whereas a penalty or sanction that the State imposes simply as a means to collect a debt for a pecuniary loss may be discharged in bankruptcy—and once it is discharged, a state trial court may not order that a defendant pay that debt in the form of restitution. In this brief, *Amici* propose a multi-factor test that balances the competing principles and permits

a court to distinguish permissible restitution obligations from those that impermissibly infringe on federal discharge relief.

The Superior Court, misapplying the United States Supreme Court's decision in *Kelly v. Robinson*, found that a previously issued bankruptcy discharge could be ignored. Unlike in *Kelly*, however, the creditor here used Pennsylvania's criminal justice system to end-run a previously issued discharge of the underlying debt by means of a compensatory—not rehabilitative—restitution provision. When creditors have appropriate notice of the bankruptcy proceeding, and therefore have the statutory right to contest those proceedings, they must avail themselves of that forum under federal law. Likewise, when a restitution statute is compensatory, it may not be used to end-run a discharge. Courts have traditionally prohibited creditors from using the state criminal process to collect an otherwise dischargeable debt under the guise of restitution, and that principle applies fully in this case. *See, e.g.*, *In re Brown*, 39 B.R. 820, 829 (Bankr. M.D. Tenn. 1984).

Amici suggest that the Court evaluate the use of the remedy of criminal restitution in cases of this kind within the framework of a five-part test: (1) whether the restitution obligation was imposed after the debtor initiated a bankruptcy case or received a bankruptcy discharge, (2) whether the beneficiaries of the restitution obligation had notice of the debtor's bankruptcy proceeding and therefore an opportunity to assert their rights and object to the discharge of their claims, (3)

whether the statute, rule, or judgment imposing the restitution obligation is compensatory or rehabilitative in nature, (4) whether the proceeding resulting in the imposition of the restitution obligation was initiated at the request of creditors of the debtor, and (5) whether the prosecutor's office conducted an independent investigation of the criminal charges. Courts should utilize these factors to distinguish cases where the State is prosecuting an individual for a crime in furtherance of its criminal justice interests from cases where the State is prosecuting someone to collect a previously discharged debt, which is improper. Because these factors raise factual questions not addressed by the lower courts, this Court should remand the matter for application of this test in light of the circumstances of the case.

Application of the test proposed here would not provide refuge for criminals seeking to avoid compensating their victims. The Bankruptcy Code itself has a number of provisions that serve to "prevent a debtor from retaining the benefits of property obtained by fraudulent means and to ensure that the relief intended for honest debtors does not go to dishonest debtors." 4 COLLIER ON BANKRUPTCY ¶ 523.08 (Richard Levin and Henry Sommer eds., 16th ed. 2018). The multi-factor balancing test *Amici* propose would prevent creditors from improperly pursuing criminal charges as a way to coerce payment of previously discharged debt, effectively end-running the federal bankruptcy system. *See In re Williams*, 438 B.R. 679, 692 (10th Cir. B.A.P. 2010) (recognizing that "there are instances where a

creditor may in fact violate the discharge injunction by seeking criminal prosecution in bad faith in order to 'coerce' the payment of a discharged debt"); P. Steven Kratsch and William E. Young, *Criminal Prosecutions and Manipulative Restitution: The Use of State Criminal Courts for Contravention of Debtor Relief*, ANNUAL SURVEY OF BANKR. LAW 5, 1-3 (Sept. 1984). *Amici* submit that the proposed test is an appropriate means of balancing the relevant interests.

ARGUMENT

A. IN RESOLVING THIS CONTROVERSY, THE COURT SHOULD TAKE INTO ACCOUNT THE COMPETING INTERESTS OF STATE CRIMINAL LAW AND FEDERAL BANKRUPTCY RELIEF.

1. States Have a Valid Interest in Exercising Their Police and Regulatory Powers for Legitimate State Purposes.

States have a legitimate interest in exercising their police powers to establish and maintain their own systems of justice. To that end, the Constitution preserves significant authority for the States to make civil and criminal laws. *See* U.S. CONST. AMEND. X. Courts likewise recognize that a State has the responsibility "to protect its citizens by enforcing its criminal statutes and to rehabilitate an offender by imposing a criminal sanction intended for that purpose." *Kelly*, 479 U.S. 36, at 52. Accordingly, federal courts often refrain from interfering with matters of state criminal law. *See Younger v. Harris*, 401 U.S. 37, 46 (1971). A State's interest in enforcing its own laws, however, is not the only constitutional and policy consideration at play in this proceeding.

2. Congress Has a Legitimate Interest in Providing for the Discharge of Debts in Bankruptcy

Article I of the Constitution provides that Congress shall have the power "[t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States." U.S. CONST. ART I, § 8, cl. 4. Moreover, the Supremacy Clause gives federal bankruptcy law priority over conflicting state law. U.S. CONST. ART. VI.; *see Perez*, 402 U.S. at 649 (when a state statute frustrates or acts as an obstacle to the realization of the objectives of the federal bankruptcy laws, the state statute is invalid); *Matter of Davis*, 691 F.2d 176, 178 (3d Cir. 1982) (in a case involving a debtor accused of writing bad checks, cautioning that the imposition of "a mandatory restitution penalty in contravention of the bankruptcy court's discharge order . . . may indeed raise serious questions under the Supremacy Clause. . . .").

Discharge of debts is among the core elements of federal bankruptcy policy. A primary goal of the Bankruptcy Code is to provide the debtor with a fresh start, and central to the fresh start is the discharge of preexisting debts. As the Supreme Court has elaborated, the purpose of the bankruptcy discharge is to relieve an insolvent debtor "from the weight of oppressive indebtedness, and (permits) him to start afresh . . . ." *United States v. Kras*, 409 U.S. 434, 457 (1973) (quoting *Williams v. U.S. Fid. & Guar. Co.*, 236 U.S. 549, 554-55 (1915)). Likewise, "[t]his purpose . . . has been again and again emphasized by the courts as being of public as well as private interest" by giving insolvent debtors "a new opportunity in life and a clear

field for future effort, unhampered by the pressure and discouragement of pre-existing debt." *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934). Congress has similarly acknowledged the benefits of the debtor's discharge, allowing most debts owed to the federal government and other governmental entities to be discharged. *See* 11 U.S.C. § 523; *FCC v. NextWave Personal Commc'ns Inc.*, 537 U.S. 293, 303 (2003).[1]

So important is the discharge that the Bankruptcy Code prevents individuals from waiving it *ex ante* at the time they incur a debt, *see* 11 U.S.C. § 524(a), and likewise places substantial *ex post* restrictions on the ability of debtors to waive the discharge with respect to particular debts through "reaffirmation" after filing for bankruptcy relief. *See id.* § 524(c).[2] Even where a debtor wishes to waive his right to a discharge through reaffirmation, strict protective provisions ensure that it does not impose an undue hardship on either the debtor or the debtor's dependents. *See*

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[1] *FCC v. NextWave Personal Commc'ns Inc.* was decided under 11 U.S.C. § 525, which was intended to enhance discharge rights and prevent discrimination against the debtor based upon nonpayment of a discharged debt. Section 525 was intended to codify and expand the Supreme Court's holding in *Perez v. Campbell*.

[2] "A 'reaffirmation agreement,' . . . is an agreement between a holder of a claim and the debtor, the consideration for which, in whole or in part, is based on a debt that is dischargeable in a case under the Bankruptcy Code. Reaffirmation represents the only vehicle through which an otherwise dischargeable debt can survive the successful completion of Chapter 7 proceedings, and an enforceable reaffirmation agreement makes a debtor remain personally obligated after discharge for a debt which is otherwise dischargeable." 8B C.J.S. *Bankruptcy* § 1093 (2012).

11 U.S.C. § 524(c)(3)(B); *Renwick v. Bennett (In re Bennett)*, 298 F.3d 1059, 1066-67 (9th Cir. 2002).

To enforce the bankruptcy discharge, section 524 of the Bankruptcy Code establishes an automatic injunction. It provides that a discharge "voids any judgment at any time obtained, to the extent that such judgment is a determination of the personal liability of the debtor with respect to any debt discharged," and directs that the discharge "operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover or offset any such debt as a personal liability of the debtor, whether or not discharge of such debt is waived." 11 U.S.C. § 524(a)(1) & (2). The discharge injunction protects the bankruptcy discharge and ensures the debtor's fresh start.

Recognizing the significance of the bankruptcy discharge, courts have adopted a number of practices to facilitate it. First, the Supreme Court has long recognized that any "exceptions to the operation of a discharge thereunder should be confined to those plainly expressed," *Gleason v. Thaw*, 236 U.S. 558, 562 (1915), and has likewise narrowly construed discharge exceptions to promote the federal "fresh start" goal. *Kawaauhau v. Geiger*, 523 U.S. 57, 62 (1998); *see also Bullock v. BankChampaign, N.A.*, 569 U.S. 267 (2013); Deborah A. Ballam, *Kelly v. Robinson: An Erosion of the Fresh Start Concept for Debtors in Bankruptcy*, 32 ST. LOUIS U. L.J. 103, 116-17 (1987) (internal citations omitted).

Second, the Supreme Court has determined that States are generally bound by the bankruptcy discharge. *Tennessee Student Assistance Corp. v. Hood*, 541 U.S. 440, 448 (2004) ("Under our longstanding precedent, States, whether or not they choose to participate in the proceedings, are bound by a bankruptcy court's discharge order no less than other creditors."). If creditors could end-run the bankruptcy discharge by pursuing state criminal charges, then the discharge, and the fresh start it promises, would in many instances be eliminated, or at least substantially impaired. *See* Kratsch and Young, *Criminal Prosecutions and Manipulative Restitution: The Use of State Criminal Courts for Contravention of Debtor Relief*, at 3.

This Court should not allow these federal bankruptcy interests to be subverted by private creditors hijacking the state criminal justice system to collect on previously discharged debts. The courts often encounter cases where a business relationship has gone awry and one of the parties has filed for bankruptcy, *see, e.g.*, *In re Johnson*, 2012 WL 3905176 (Bankr. S.D. Ala. Sept. 7, 2012,), or consumers who have fallen behind on their payments due to unforeseen financial hardship. *See generally* Creola Johnson, *Prosecuting Creditors and Protecting Consumers: Cracking Down on Creditors that Extort via Debt Criminalization Practices*, DUKE J. OF L. & CONTEMPORARY PROBLEMS (2017). Despite receiving notice of bankruptcy proceedings, the creditors in these cases failed to assert their rights in the

bankruptcy forum. Rather, after the debt had been discharged, the creditors utilized the state justice system to pursue criminal charges wherein they sought restitution for the debt previously discharged. The courts have seen through these veiled attempts at end-running the bankruptcy court's discharge and authority, and this Court should recognize and address the inappropriate nature of such behavior.

B. THE FEDERAL BANKRUPTCY CODE PROVIDES VICTIMS OF FINANCIAL WRONGDOING WITH AMPLE REMEDIES AND PREVENTS WRONG-DOERS FROM SEEKING REFUGE IN BANKRUPTCY.

The Bankruptcy Code itself balances discharge relief against the competing interests of the victims of financial wrongdoing. First, the Code and the Federal Rules of Bankruptcy Procedure prescribe various safeguards, such as their notice requirements and provisions for an opportunity to be heard, ensuring that creditors may protect their rights. Second, the Code lists various types of debts that are not dischargeable. 11 U.S.C. § 523(a). For example, where a creditor raises the issue, the Code excepts from discharge a debt that has been obtained through fraud or deception, 11 U.S.C. § 523(a)(2)(A) & (c), or obtained for willful or malicious injury by the debtor. 11 U.S.C. § 523(a)(6) & (c). In fact, a creditor alleging that a discharge was obtained fraudulently, or without notice, has enumerated rights to pursue its revocation in the bankruptcy court, rather than through an end-run in the state courts. 11 U.S.C. § 727(d). These provisions encourage and require creditors to assert their rights in the bankruptcy court, rather than attempting to defy the

discharge injunction by proceeding in state court. *See* 11 U.S.C. § 524(a)(1) & (2). And what creditors are prohibited from doing directly, the States are prohibited from doing indirectly for the benefit of creditors through the exercise of their police and regulatory powers. *See Perez*, 402 U.S. at 649.

1. **The Code's Notice and Other Provisions Provide Ample Opportunity for Victims of Financial or Economic Wrongdoing, Who Therefore Qualify As Creditors, to Be Heard and Participate in the Bankruptcy Proceeding.**

The Bankruptcy Code's notice requirements provide any creditor, including any victim of financial wrongdoing, ample opportunity to be heard and object to the discharge of a debt. In addition to the notice provided to all creditors at the beginning of the case, section 342 of the Code, and the relevant Federal Rules of Bankruptcy Procedure, specify a host of measures designed to ensure notice to all parties interested in the debtor's bankruptcy proceeding. 11 U.S.C. § 342; *see*, *e.g.*, Fed. R. Bankr. P. 2002, 5008. Rule 2002(f) provides that creditors receive notice of the deadline to file a complaint objecting to the dischargeability of debt. The court sends all creditors Official Form 309 to "give notice to creditors of the bankruptcy case, the time, date and location of the meeting of creditors, the time for filing various documents in the case, instructions for filing proofs of claim, and other information concerning the case." Instructions, Form 309 (A-I) (December 2017). Even in cases in which the debtor does not have a creditor's information sufficient to permit actual notice by mail, the debtor is generally required to attempt notice, including through

publication. *See* 3 COLLIER ON BANKRUPTCY ¶ 342.02 (Richard Levin and Henry Sommer eds., 16th ed. 2018) (citing H.R. Rep. No. 595, 95th Cong., 1st Sess. 331 (1977), *reprinted in* App. Pt. 4(d)(i)); *Chemetron Corp. v. Jones*, 72 F.3d 341, 346 (3d Cir. 1995).

After receiving notice, creditors may file claims for any sums they are owed and may challenge the debtor's discharge. *See, e.g.*, 11 U.S.C. §§ 501, 502 & 523. For example, a creditor may object to the discharge of any debt to the extent it is for money obtained by false pretenses, a false representation, actual fraud, or for willful and malicious injury, and such debts will not be dischargeable if challenged. 11 U.S.C. § 523(a)(2)(A), (a)(6) & (c). A creditor may also object to the debtor's discharge in its entirety under certain circumstances. *See* 11 U.S.C. § 727(a). These notice and other requirements ensure the satisfaction of basic principles of due process, as reflected "in section 523(a)(3), which precludes discharge of a debt if a creditor did not receive notice in time to file (1) a proof of claim when there is a deadline for filing claims or (2) a complaint challenging dischargeability of a debt if the creditor could otherwise have successfully filed such a complaint." 3 COLLIER ON BANKRUPTCY ¶ 342.02. Furthermore, in the event that such a creditor does not receive notice, a debt for fraud or willful and malicious injury can be pursued after bankruptcy in state or federal court. 11 U.S.C. § 523(a)(3). These provisions demonstrate that the Bankruptcy Code was thoughtfully and deliberately written to

reflect the core concepts of due process for the creditors and provide protection of their rights.

2. The Bankruptcy Code Provides Ample Exceptions to Dischargeability to Protect the Interests of Victims of Financial Wrongdoing.

The Bankruptcy Code includes many exceptions to the dischargeability of a debt to the extent the debt is the product of dishonest or criminal activity. As referenced above, debts for money, property, or services, or an extension, renewal or refinancing of credit to the extent obtained by false pretenses, a false representation or actual fraud are not dischargeable under section 523(a)(2). The "purposes of the provision are to prevent a debtor from retaining the benefits of property obtained by fraudulent means and to ensure that the relief intended for honest debtors does not go to dishonest debtors." 4 COLLIER ON BANKRUPTCY ¶ 523.08. In addition to section 523(a)(2), "section 527(a)(4) exempts debts that stem from embezzlement or larceny; [and section] 523(a)(6) exempts debts that stem from 'willful and malicious injury by the debtor to another entity or to the property of another entity.'" *Matter of Towers*, 162 F.3d 952, 956 (7th Cir. 1998). As the Seventh Circuit commented in *Towers*, these "three exemptions cover the gamut of crimes, [and t]he only reason [the state and debtor's victims] cannot take advantage of these exclusions from discharge is that they snoozed through [the] bankruptcies." *Id.* As that case holds, creditors have an obligation to pursue their rights and

remedies in the bankruptcy forum and should not be rewarded for effectively sleeping on their rights

Thus, the Bankruptcy Code provides numerous safeguards to prevent a criminal debtor from obtaining refuge in bankruptcy and ample opportunity for creditors to protect their interests. The Code likewise consolidates all debtor and creditor issues in one venue, allowing the federal bankruptcy judge to examine all of the relevant factors before ruling on discharge and other debt relief issues.[3] When a creditor with notice fails to participate in the federal bankruptcy case, she necessarily forfeits her opportunity and ability to assert her rights and should not be allowed to end-run a final discharge by pursuing criminal remedies to collect a discharged debt.

C. THE COURT SHOULD TAKE THIS OPPORTUNITY TO ESTABLISH A LEGAL STANDARD THAT APPROPRIATELY RESPECTS THE STATE'S INTERESTS IN IMPOSING RESTITUTION OBLIGATIONS WHILE AT THE SAME TIME RESPECTING THE PURPOSE AND AUTHORITY OF THE FEDERAL BANKRUPTCY DISCHARGE.

[3] The power to determine dischargeability was granted to bankruptcy courts by the 1970 Amendments to the Bankruptcy Act in order to prevent creditors from asserting claims of fraud in state civil courts after bankruptcy. Congress intended to take the determinations governed by 11 U.S.C. § 523(c) away from state courts and grant exclusive jurisdiction in the bankruptcy courts. *Spilman v. Harley*, 656 F.2d 224, 226 (6th Cir. 1981) (citing *Brown v. Felsen*, 442 U.S. 127 (1979)).

1. **This Case is Markedly Different from *Kelly*, which does not Dictate the Outcome Here.**

a. The relative timing of the bankruptcy and the filing of the restitution action are entirely different in the case before the Court.

Perhaps the most important difference between the facts of this case and *Kelly* is the timing of the bankruptcy filing. In *Kelly*, the defendant filed for bankruptcy after the court ordered restitution. 479 U.S. at 38-39. Here, however, Petitioner filed for bankruptcy before any criminal charges were filed. *Commonwealth v. Petrick*, 2018 WL 947167, *1 (Pa. Super. Ct. Feb. 20, 2018). This difference is crucial because, as noted above, the Bankruptcy Code provides significant creditor protections, and creditors are both encouraged and required to pursue their debts in the bankruptcy court. *Spilman v. Harley*, 656 F.2d 224, 226 (6th Cir. 1981) (citing *Brown v. Felsen*, 442 U.S. 127 (1979)). Regardless of whether the criminal charges are filed during the bankruptcy proceedings or following the bankruptcy discharge, creditors are limited to collecting debts in the proper venue and through proper channels. When creditors do not avail themselves of the bankruptcy process, any subsequent criminal action for the same debt previously discharged should be viewed as an improper and impermissible end-run around the federal bankruptcy discharge

b. Unlike the restitution statute in *Kelly*, Pennsylvania's restitution statute at issue here is not rehabilitative.

Beyond the chronological differences, the statutes at issue in *Kelly* and in this case are also fundamentally different. While the Connecticut statute addressed in *Kelly* was rehabilitative, the type of restitution authorized by 18 Pa.C.S. § 1106 is purely compensatory and serves no rehabilitative purpose. While recent cases from the Superior Court and this Court have continued to characterize restitution as primarily rehabilitative in nature, they import that language and view from a time before the statute was substantially rewritten in 1995. For example, this Court recently noted "the well-established principle 'that the primary purpose of restitution is rehabilitation of the offender.'" *Commonwealth v. Veon*, 150 A.3d 435, 466-67 (Pa. 2016) (quoting *Commonwealth v. Runion*, 662 A.2d 617, 618-19 (Pa. 1995)). But *Runion* was from a different era, one in which restitution under section 1106 could only be imposed in "the amount that the offender can afford to pay." *Runion*, 662 A.2d at 619. That is no longer the case, and restitution no longer serves the rehabilitative purpose it once did. Rather, restitution now focuses on compensating victims for their loss.

Prior to 1995, cases from this Court and the Superior Court made it clear that restitution imposed under section 1106 had to be tailored to the financial resources of the defendant. *See*, *e.g.*, *Commonwealth v. Wood*, 446 A.2d 948, 949-50 (Pa. Super. Ct. 1982) (sentencing court must ensure "that the amount awarded does not exceed the defendant's ability to pay"). Tying restitution to the defendant's ability

to pay served a "rehabilitative goal" by "impressing upon the offender the loss he has caused and his responsibility to repair that loss as far as it is possible to do so." *Commonwealth v. Fuqua*, 407 A.2d 24, 26 (Pa. Super. Ct. 1979) (citation omitted). Indeed, this was key to rehabilitation, as a "concern that the victim be fully compensated should not overshadow its primary duty to promote the rehabilitation of the defendant." *Id.*

Today, section 1106 restitution no longer serves this rehabilitative goal because it has been separated from the defendant's financial ability to pay. Section 1106(c) requires that the sentencing court order "full restitution . . . so as to provide the fullest *compensation* for the loss." 18 Pa.C.S. § 1106(c) (emphasis added); *see also* 42 Pa.C.S. § 9721(c) (the sentencing court "shall order the defendant to compensate the victim of his criminal conduct for the damage or injury that he sustained"). This restitution is imposed *without* consideration of the "current financial resources of the defendant," as the court is prohibited from considering whether the defendant will be able to afford that restitution. 18 Pa.C.S. § 1106(c); *see Commonwealth v. Colon*, 708 A.2d 1279, 1283 (Pa. Super. Ct. 1998) (defendant's ability to pay restitution is relevant only if the defendant defaults). These changes were implemented shortly before this Court's decision in *Runion* and did not factor into that decision, but they should be considered here. *See Veon*, 150 A.3d at 467.

This Court has never addressed whether the post-amendment section 1106 remains rehabilitative. Instead, in cases like *Veon*, the Court has simply looked back to the pre-1995 cases and repeated their reasoning. As section 1106(c) now makes clear, however, the purpose of restitution under that section is to provide the victim with "compensation"—not to rehabilitate the defendant. Defendants are no longer "called upon to make reasonable sacrifices in order to compensate those who have sustained losses as a result of his criminal conduct" because the court has no ability to know what constitutes a "reasonable sacrifice." *Wood*, 446 A.2d at 950. Instead, the "rehabilitative goal is defeated" because defendants in many cases "cannot hope to comply" with the restitution order. *Id*. The result is that defendants continue to owe large amounts of restitution: in cases that were adjudicated in 2008, only 27% of the $107,512,991 of restitution owed in criminal cases has been collected.[4] As the *Fuqua* court warned, the rehabilitative purpose of restitution has been "disserved." *Fuqua*, 407 A.2d at 26.

In contrast to the purely compensatory section 1106 restitution, the General Assembly has maintained a form of *rehabilitative* restitution applied as a condition of probation. Section 9754(c)(8) provides that a condition of probation may include that a defendant "make restitution of the fruits of his crime or to make reparations,

[4] Administrative Office of Pennsylvania Courts, "Collection Rates Over Time," http://www.pacourts.us/news-and-statistics/research-and-statistics/dashboard-table-of-contents/collection-rate-of-payments-ordered-by-common-pleas-courts.

in an amount he can afford to pay, for the loss or damage caused thereby." 42 Pa.C.S. § 9754(c)(8). As the plain language makes clear, under section 9754 the State must consider the defendant's finances. This is in marked contrast to section 1106 restitution. Last year, four judges on the Superior Court acknowledged this distinction, writing: "Unlike restitution under Section 1106(a) that serves a punitive purpose, restitution ordered as a condition of probation under Section 9754(c)(8) is primarily aimed at rehabilitating and integrating a defendant into society as a law-abiding citizen and is deemed a constructive alternative to imprisonment." *Commonwealth v. Holmes*, 155 A.3d 69, 86-87 (Pa. Super. Ct. 2017) (en banc) (opinion of four judges).

As a result, the plain language of section 1106—as amended in 1995—shows that the purpose of restitution under that section is to compensate victims for their financial losses. This is not a rehabilitative purpose, and recent cases that have suggested otherwise have failed to carefully consider the transformative impact that the 1995 amendment had on the nature of restitution in Pennsylvania. *Kelly* is simply inapposite.

2. When Considering Whether a Criminal Restitution Obligation Infringes on the Bankruptcy Discharge, the Court Should Apply a Multi-Factor Test.

Based on the foregoing, and in light of the competing legal principles at stake, *Amici* propose that the Court adopt, and remand for the trial court to apply, a

balancing test evaluating the state's interest in pursuing and enforcing a restitution obligation against the federal discharge protections by considering five discrete questions. This test considers the specific circumstances surrounding the post-petition or post-discharge criminal proceeding to best determine whether the charges are brought to pursue the state's criminal justice interest or for the creditor to collect a debt under the cloak of restitution. *Williams*, 438 B.R. at 692; *In re Brown*, 39 B.R. at 829.

a. Question 1: Was the restitution obligation imposed after the debtor initiated a bankruptcy case or received a bankruptcy discharge?

A bankruptcy discharge operates as an injunction against the collection of a discharged debt. 11 U.S.C. § 524(a)(3). Given the importance of federal discharge relief, the opportunity given creditors to participate in the bankruptcy proceeding and assert their rights, and the injunction granted upon discharge, it is appropriate to consider the timing of the restitution obligation and whether it was imposed after the issuance of the discharge.

Once a discharge has been granted, the values and policies that the discharge promotes come into play and the need for their protection becomes pressing. Under these circumstances, the creditor should not be permitted to end-run the bankruptcy court's order and collect on the debt. *See, e.g.*, *Johnson*, 2012 WL 3905176 (finding that the delay of initiating criminal charges until after the bankruptcy had been

discharged was evidence of the creditor's intent to collect on its debt in violation of the discharge injunction). In addition, when the criminal proceeding is initiated after bankruptcy is filed, this may reflect an improper collection purpose. *Id.*; *see also In re Dovell*, 311 B.R. 492, 494 (Bankr. S.D. Ohio 2004) (finding that the creditor initiated the post-petition criminal proceedings to compel payment of the discharged debt). Courts should thus be suspicious when the creditors initiate criminal charges *after* the bankruptcy court has discharged the relevant debt.

b. Question 2: Did the beneficiaries of the restitution obligation have notice of the debtor's bankruptcy proceeding and therefore an opportunity to assert their rights and object to the discharge of their claims, and, if not, would notice have resulted in the denial of the discharge?

The standard should also include consideration of whether the beneficiaries of the restitution obligation had a full and fair opportunity to assert their rights as part of the debtor's bankruptcy proceeding, and if they did not, whether they would in any event have been able to object successfully to the debtor's discharge. Creditors who have slept on their rights should not be entitled to avoid the bankruptcy process by resorting to state restitution remedies, including those pursued by the State, especially if the restitution remedies are designed predominantly to compensate them for pecuniary loss. *Towers*, 162 F.3d at 956. Especially when the restitution obligation is exclusively or predominantly compensatory in nature and was initiated at the request of private creditors who had

notice of the debtor's bankruptcy proceeding but simply opted not to participate (or who participated and were not successful in the bankruptcy court), a state court should conclude that the relevant restitution obligation improperly infringes on the bankruptcy discharge. Even when no notice was provided, the court should consider whether the creditor had a basis to challenge the discharge, or whether the lack of notice was harmless error. Consideration of this factor recognizes that the federal bankruptcy courts are best suited to manage and adjudicate issues relating to notices of claims, distribution of payments, and determinations of dischargeability.

c. Question 3: Is the statute, rule, or judgment imposing the restitution obligation compensatory or rehabilitative in nature?

When considering whether a restitution obligation is predominately or purely compensatory, the Court should examine the method of calculating or determining restitution under the specific state statute. A restitution award determined based on the harm suffered by the victim should be considered compensatory in nature. In *Kelly*, the Supreme Court reasoned that the debt in question was properly nondischargeable because "the decision to impose restitution generally does not turn on the victim's injury, but on the penal goals of the State and the situation of the defendant." 479 U.S. at 52. In contrast the restitution award in this case turns entirely on the victim's injury; in fact, the trial court was forbidden from considering the defendant's circumstances. 18 Pa.C.S. § 1106(c) (courts must impose restitution "[r]egardless of the current financial resources of the defendant, so as to provide the

victim with the fullest compensation for the loss"). Furthermore, the Pennsylvania restitution statute requires that the District Attorney solicit information from the victim before making a recommendation regarding the restitution amount, and any award of restitution reduces the amount of civil damages to which the victim is entitled. *Id*. § 1106(c)(4)(i) & (g). The statute leaves no doubt that restitution under section 1106 is meant to be purely compensatory to the victim, focusing exclusively on the loss suffered. In *Kelly*, the Supreme Court did not identify any government interest served by the restitution statute it considered, other than rehabilitation. A bankruptcy discharge should not be upended by a compensatory restitution order.

d. Question 4: Was the proceeding resulting in the imposition of the restitution obligation initiated at the request of creditors of the debtor?

Because criminal restitution obligations should not be imposed simply as debt collection vehicles to avoid the bankruptcy discharge, the identity of the party who initiated the criminal proceeding is relevant in determining the nature of the restitution obligation. Depending on the circumstances, the fact that the criminal complaint is brought at the behest of the alleged victim is strong evidence that the motivation for bringing the complaint is to collect a debt. Bankruptcy courts have considered this factor in determining whether imposing a criminal restitution violates the debtor's discharge. In *In re Dovell*, the court found that the criminal complaint in that case was for the purpose of collecting a debt and therefore violated

the discharge. 311 B.R. at 495*; see also In re Burton*, 2010 WL 996537, at *4 (Bankr. W.D. Ky. Mar. 16, 2010). These cases deal with private creditors attempting to collect a previously discharged debt by pursuing criminal prosecutions for bad checks. *Dovell*, 311 B.R. at 494. There is also concern that corporations will weaponize the state criminal justice system to help them collect on missed payments under Pennsylvania's theft of leased property statute.[5] Joshua Vaughn, *Pennsylvania Prosecutors Pursue Charges for People who Fall Behind on Rent-to-own Payments*, THE APPEAL (Sept. 5, 2018) (noting that "[t]he Appeal reviewed all criminal dockets filed in the state in 2016 and found 610 cases charged under the statute largely stemming from rent-to-own companies including Aaron's and Rent-A-Center."). Furthermore, under Pennsylvania law, corporations are able to recover restitution, creating a dangerous avenue through which a corporate entity may collect a debt outside of the bankruptcy forum. 18 Pa.C.S. 1106(h) (as amended by Act 145 of 2018). Although not dispositive by itself, it is appropriate to consider the identity of the party urging the imposition of the obligation in determining whether a restitution obligation is an attempt to end-run the bankruptcy court's discharge. *See* Kratsch and Young, *Criminal Prosecutions and Manipulative Restitution: The Use of State Criminal Courts for Contravention of Debtor Relief*, at 1.

[5] Notably, Pa. R. Crim. P. 506 authorizes private criminal complaints to initiate a possible criminal proceeding.

e. Question 5: Did the prosecutor's office conduct an independent investigation of the criminal charges?

In determining the purpose of the criminal complaint, it is also appropriate to examine the level of independent investigation conducted by the state prosecutor. When the prosecutor merely accepts the complaining creditor's claims and does no independent investigation, the State is essentially acting as a collection agent for a private actor. In *In re Dovell*, the bankruptcy court found that the State's lack of independent investigation into the accuracy of the criminal allegations evidenced that the creditor initiated the criminal proceeding to collect the debt that was previously discharged in the debtor's chapter 7 case. 311 B.R. at 494-95. Furthermore, a prosecution may be in bad faith if there is reason to doubt the validity of the charges. *See Williams*, 438 B.R. at 692-93 (citing *In re McMullen*, 189 B.R. 402, 411 (Bankr. E.D. Mich. 1995)). In such cases, where "there is little likelihood of a guilty verdict being rendered, suspicions naturally arise that the prosecutor has some ulterior motive for proceeding with the case," and the prosecution may merely be a way for the creditor to coerce the debtor to pay the discharged debt. *Williams*, 438 B.R. at 693 (quoting *McMullen*, 189 B.R. at 411). A prosecutor should conduct an independent investigation to ensure the criminal charges are being brought to serve a state's interest in criminal justice rather than the private creditor's interest in collecting a discharged debt, and when no such investigation occurs, the court should be skeptical of the intention behind the criminal proceedings.

3. **The Proposed Test Is Fully Consistent with *Kelly*.**

The proposed balancing test does not ignore the concerns identified by the Supreme Court in *Kelly*. Rather, it appropriately recognizes that restitution obligations may arise in different ways and under materially different circumstances, and thus implicate the competing interests of state and federal law in different ways. When a restitution obligation is imposed after the issuance of a lawfully obtained discharge upon due and proper notice and an opportunity to be heard, it constitutes an impermissible end-run around the bankruptcy discharge, particularly if restitution was sought at the behest of a creditor. Likewise, when a restitution obligation is compensatory, rather than rehabilitative, it constitutes a debt dischargeable under the Bankruptcy Code. *Amici* therefore ask that the Court adopt the proposed multi-factor balancing test to distinguish legitimate and illegitimate uses of restitution obligations in light of the particular federal concerns at issue here.

CONCLUSION

For the foregoing reasons, the Court should adopt the test proposed above and remand the matter to the trial court to apply the test in light of the facts and circumstances of this case.

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CERTIFICATE OF COMPLIANCE WITH WORD LIMIT

I certify pursuant to Pa.R.A.Ps. 531 and 2135 that this brief does not exceed 7,000 words.

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